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ECONOMIC TALKING POINTS

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The Fed is now in a real quandary!

Trouble ahead: The odds of another quarter point cut in December has diminished. There are two reasons for that.

Let's look at the first, the latest CPI data, and then move on to the second reason, which deals with the more ominous outlook for consumer prices.

October's headline CPI bounced up to 2.6% over the year, the highest since July. Virtually every major component contributed to that uptick, including food, energy services (electricity and piped in natural gas), used cars and trucks, shelter, transportation and medical services. Motor vehicle insurance alone surged 14% from its ago level. The price of eggs shot up more than 30% compared to last October.

Core inflation, which excludes food and energy, seems stuck at 3.3%, after touching 3.2% in August. Both headline and core have thus taken a step back from reaching the Fed's target of 2%.

It is, however, mostly the second reason why December's monetary policy meeting will be problematic.

Let me be frank here. There were moments prior to the November election when I would tell clients we were better off making economic forecasts based on answers from the playful round 8-ball. After all, we had two presidential candidates with profoundly different strategies for the economy in a reportedly tight race. But with the election over, it is now possible to ditch that otherwise useless toy.

Donald Trump -- whether you voted for him or not -- has won and he can arguably proclaim achieving an electoral mandate, along with a sweeping GOP win in Congress.

With that singular accomplishment, the bands of uncertainty have now narrowed and we are in a better position to project the direction of inflation.

Given all that President-elect Trump has promised to do quickly --- such as hike tariffs, cut taxes further and slash immigration --- one can easily foresee a re-acceleration of inflation next year. The Federal Reserve is now in a real quandary. Does it really want to reduce rates next month, only to possibly hike them again in 2025? I don't think so.

Higher tariffs, no matter how flawed the rationale for it is, will take place early in 2025. And we've already seen a number of US importers --- including Stanley Black & Decker, AutoZone and Walmart --- warn they are prepared to pass those costly duties on to consumers.

Thus, while the Fed has achieved much success in bringing down inflation the last year and a half, their victory could well turn out to be ephemeral. Case in point: The bond market, always hypersensitive to any whiff of inflation, has shown its concern. The yield on 10-year treasuries jumped to 4.43% yesterday, up about 70 basis points since the start of October!

A rebound in inflation will therefore be difficult to avoid. History has repeatedly warned us about the corrosive effects tariffs have on prices. Economic models will shortly flash those same inflation warning lights for 2025. Our model shows the boost in tariffs, along with an expansive fiscal policy, will push both headline and core CPI to 4% next year.

For now, all eyes should be laser focused for signs that inflation expectations are about to be unanchored.